



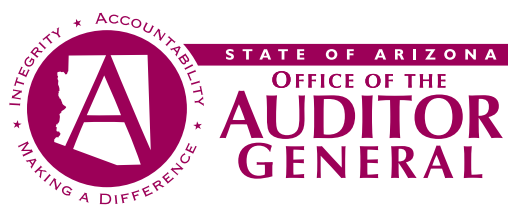
A REPORT
TO THE
ARIZONA LEGISLATURE

Accounting Services Division

Compliance Review

Phoenix Elementary School District No. 1

Year Ended June 30, 2002



Debra K. Davenport
Auditor General

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DEBRA K. DAVENPORT, CPA
AUDITOR GENERAL

STATE OF ARIZONA
OFFICE OF THE
AUDITOR GENERAL

WILLIAM THOMSON
DEPUTY AUDITOR GENERAL

January 14, 2004

Governing Board
Phoenix Elementary School District No. 1
1817 North 7th Street
Phoenix, AZ 85006-2133

Members of the Board:

We have reviewed the District's single audit reports and Uniform System of Financial Records (USFR) Compliance Questionnaire for the year ended June 30, 2002, to determine whether the District substantially complied with the USFR.

As a result of our review, we noted significant deficiencies in internal controls that indicate the District had not complied with the USFR. District management should implement the recommendations we have described in this report within 90 days after the date of this letter. We have communicated specific details for all deficiencies to management for correction.

During the 90-day period, the District may request a meeting to discuss these recommendations with my Office and the Arizona Department of Education by calling Magdalene Haggerty, Accounting Services Director, or Gregg Rickert, Accounting Services Manager.

A member of my staff will call the Business Manager in several weeks to discuss the District's action to implement these recommendations. After the 90-day period, my staff will schedule an on-site review of the District's internal controls to determine whether the District is in substantial compliance with the USFR. Our review will cover the deficiencies we have communicated to management as well as any other internal control deficiencies we are aware of at the time of our review.

Sincerely,

Debra K. Davenport
Auditor General

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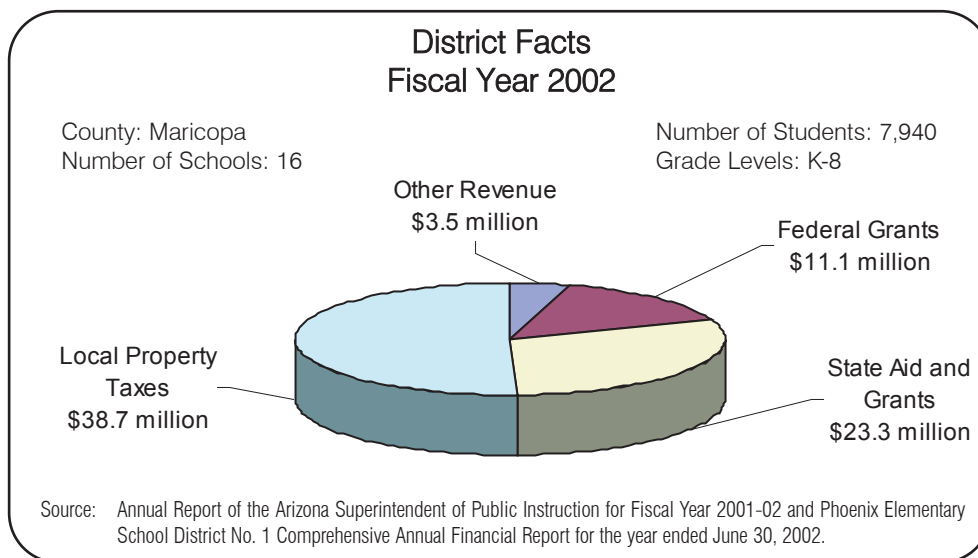
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INTRODUCTION

Phoenix Elementary School District No. 1 is accountable to its students, their parents, and the local community for the quality of education provided. The District is also financially accountable to taxpayers for more than \$76 million it received in fiscal year 2001-02 to provide this education.

The District should use effective internal controls to demonstrate responsible stewardship for the tax dollars it receives. These controls are set forth in the *Uniform System of Financial Records* (USFR), a joint publication of the Office of the Auditor General and the Arizona Department of Education. The policies and procedures in the USFR incorporate finance-related state and federal laws and regulations, and generally accepted accounting principles applicable to school districts. Districts are legally obligated to comply with USFR requirements, and doing so is good business practice.

As a result of our review of the District's single audit reports and USFR Compliance Questionnaire for the year ended June 30, 2002, we determined that the District had failed to comply with the USFR. We noted certain deficiencies in controls that the District's management should correct to ensure that it fulfills its responsibility to establish and maintain adequate financial stewardship, and to comply with the USFR. Our recommendations are described on the following pages.



The District must follow competitive purchasing requirements

In many cases, the District did not comply with School District Procurement Rules and USFR guidelines when purchasing goods and services.

School District Procurement Rules for competitive sealed bidding and USFR guidelines for purchases below the competitive sealed bid threshold promote open and fair competition among vendors. This helps ensure that districts receive the best possible value for the public monies they spend. However, the auditors found that the District did not always follow the School District Procurement Rules or the USFR guidelines. For example, the District did not always document when the invitations for bids were issued, include all required information in the invitations for bids, document the Governing Board's determination for a sole source purchase, or obtain oral price quotations for purchases requiring them.

In addition, for all seven competitive sealed proposals tested, the District did not determine in writing that using proposals would be more beneficial to the District than using competitive sealed bids.

Recommendations

To strengthen controls over competitive purchasing, the District should establish and follow the policies and procedures listed below:

- Obtain competitive sealed bids or proposals, as appropriate, for purchases of construction, materials, or services exceeding \$32,700.
- For competitive sealed bids, retain documentation of when invitations for bids were issued and time- and date-stamp envelopes for bids submitted. Also, the District should include a statement in the invitations for bids that submitted bids will be available for public inspection following the contract's award, and prepare bid tabulation worksheets when opening bids.
- For competitive sealed proposals, obtain written documentation from the Governing Board that the use of competitive sealed bids is not beneficial to the District before making purchases using competitive sealed proposals. The District should identify in the requests for proposals the relative importance of price and other evaluation factors and document in writing the proposal determined to be most advantageous to the District based on the factors set forth in the requests. Then, the District should award the contract to that vendor and maintain supporting documentation of the reasons for that award.
- Only award a contract for a material, service, or construction item without competition if the District's Governing Board determines in writing that there is

School District Procurement Rules provide the requirements for:

- Competitive sealed bids for goods and services in excess of \$32,700.
- Competitive sealed proposals for goods and services when factors other than the lowest cost are appropriate.
- Sole source and emergency procurements and other exceptions.

only one vendor from which to purchase the item and retains that written determination with other supporting documents. Sole source procurement should be avoided, except when no reasonable alternative vendor exists.

- Obtain oral price quotations from at least three vendors for purchases estimated to cost between \$5,000 and \$15,000. If the District cannot obtain three price quotations, it should document the vendors contacted and their reasons for not providing quotations.

USFR guidelines require:

- Oral price quotations for purchases between \$5,000 and \$15,000.
- Written price quotations for purchases between \$15,000 and \$32,700.

The District should ensure the accuracy of its accounting records

The District's Governing Board depends on accurate information to fulfill its oversight responsibility. The District should also report accurate information to the public and agencies from which it receives funding. To achieve this objective, management should ensure that transactions are recorded in the appropriate accounts and adjustments to the accounting records for reconciling items are prepared and posted in a timely manner. However, the District did not fully accomplish this objective. Specifically, the auditors indicated numerous expenditures were misclassified in the District's accounting records. Also, the District did not prepare adjustments for errors totaling more than \$220,000 that were identified when the County School Superintendent (CSS) reconciled its cash balances to the County Treasurer's cash balances.

Over \$220,000 in reconciling items identified in the monthly cash reconciliations to the County Treasurer's balances were not posted to the District's accounting records.

Recommendations

The following procedures can help the District to record and report accurate financial information:

- Classify all revenues and expenditures in accordance with the USFR Chart of Accounts (§III).
- Adjust revenues, expenditures, and cash balances monthly for errors identified in the reconciliations of the CSS' records to the County Treasurer's records.

The District's capital assets list should be updated annually

The District's financial statements indicate the District had over \$4.5 million in capital asset additions; however, the District did not update its capital assets list.

The District has invested a significant amount of money in its capital assets, which consist of land, buildings, and equipment. Effective stewardship requires the District to have an accurate list of these assets and to document the values assigned to them. However, as mentioned in the auditors' report, the District did not maintain a capital assets additions list for fiscal year 2001-02 and, therefore, was unable to update its capital assets list. As a result, the District was unable to reconcile capital expenditures to items added to the capital assets list, or the current year's capital assets list to the prior year's list to help ensure that the list had been accurately adjusted for items acquired and disposed of.

Recommendations

To help ensure that the District maintains an accurate capital assets list, district staff should:

- Update the capital assets list annually for items purchased, disposed of, or transferred to other locations.
- Reconcile items added to the capital assets list during the fiscal year to capital expenditures for that year, and make all necessary corrections.
- Reconcile the prior year's list to the current year's list, and make all necessary corrections.

The form on USFR page VI-E-13 may be used to reconcile capital asset additions to capital expenditures.

The form on USFR page VI-E-14 may be used to reconcile last year's capital assets list to this year's list.

The District should maintain accurate records for employee benefits

Employee benefits are a major portion of the District's payroll expenditures and, therefore, it is essential that the District maintain accurate accounting records for those expenditures. However, the auditors stated that the District's accounting records and employee files lacked some of the information and the documents needed to support employee benefit deductions, reimbursements, and payments. Lacking was a list of retired employees eligible for medical insurance assistance payments from the Arizona State Retirement System, and health insurance and retirement enrollment forms. Therefore, the District could not determine the correct premiums to remit to health insurance companies or the amounts to be reimbursed

The District overpaid insurance premiums by approximately \$450,000, but was only reimbursed for about \$150,000 of the overpayments.

by retirees and former employees. As a result, the District overpaid two health insurance companies by approximately \$458,500 and failed to collect approximately \$40,000 owed by retirees and former employees. Due to provisions in the health insurance contracts requiring notice of an employee's termination within 60 days of the actual termination, the District was unable to recover approximately \$300,000 of the overpayments. Because these overpayments provided insurance coverage for employees well past their termination dates, these payments may constitute gifts of public monies in violation of Article IX, §7 of the Arizona Constitution.

In addition, the District did not monitor hours worked by employees who did not contribute to the retirement system to determine if and when those employees became eligible for the retirement system.

Recommendations

To help ensure that all employees receive their entitled employee benefits and the District only pays the amounts it owes, the District should follow the procedures listed below:

- Maintain the required employee benefit deduction forms in employee files as a basis for preparing payroll vouchers and reports, and verify health insurance billings.
- Maintain files for retirees' and former employees' health insurance benefits as a basis for verifying reimbursements.
- Have a second employee verify that payments made to health insurance companies are accurate by comparing them to the District's list of eligible employees, employee deductions, and reimbursements.
- Monitor the hours worked by hourly employees to determine if and when they become eligible for the retirement system. When employees become eligible, notify them of their status change, have them fill out the appropriate forms, and withhold retirement contributions from their pay.